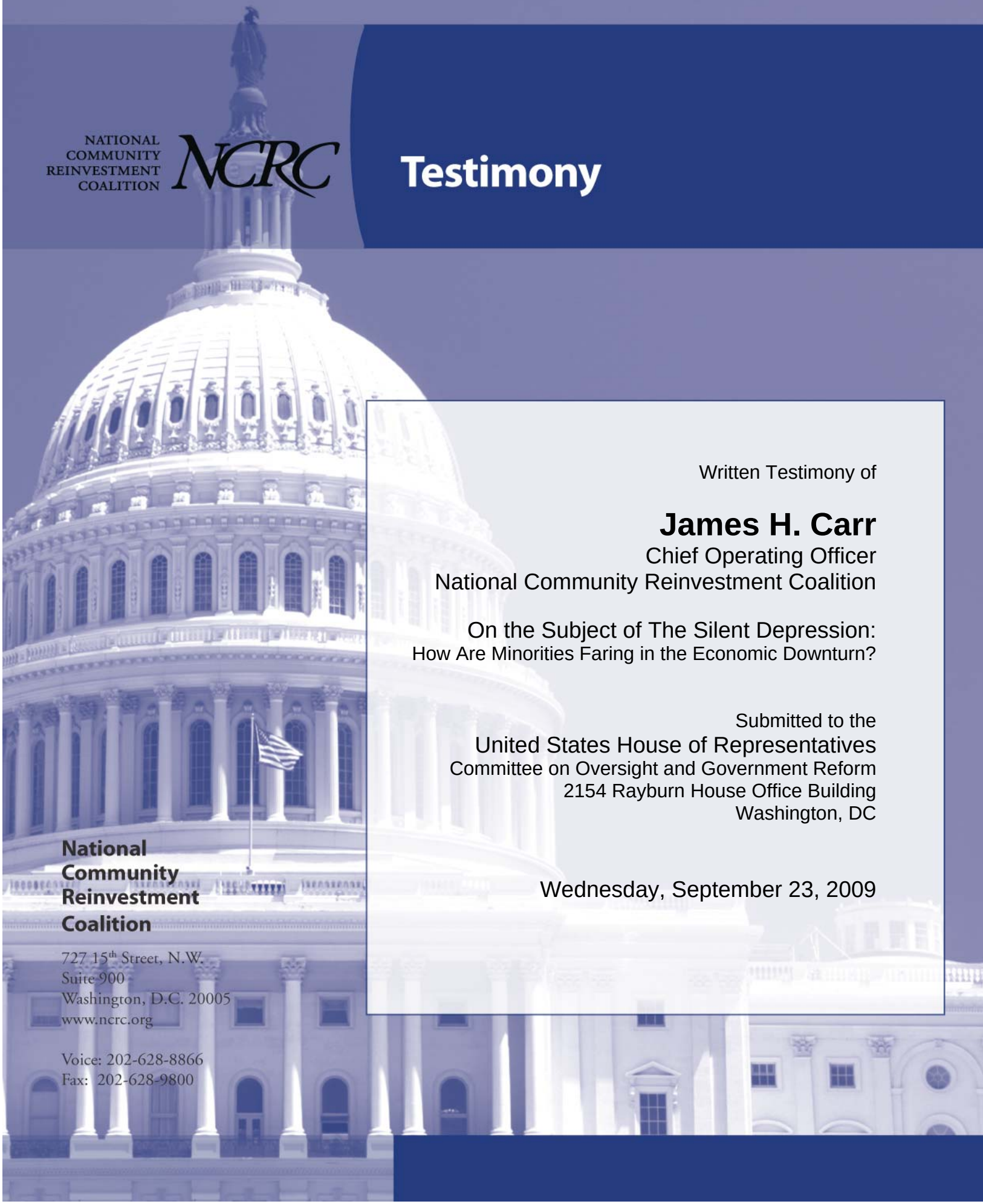


NATIONAL COMMUNITY REINVESTMENT COALITION

NCRC

Testimony

Written Testimony of

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On the Subject of The Silent Depression:
How Are Minorities Faring in the Economic Downturn?

Submitted to the
United States House of Representatives
Committee on Oversight and Government Reform
2154 Rayburn House Office Building
Washington, DC

Wednesday, September 23, 2009

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Introduction

Good morning, Chairman Towns, Ranking Member Issa, and members of the committee. On behalf of the National Community Reinvestment Coalition, I am honored to speak with you today about the racial dimensions of the economic crisis.

NCRC is an association of more than 600 community-based organizations that promotes access to basic banking services, including credit and savings, to create and sustain affordable housing, job development, and vibrant communities for America's working families. NCRC is also pleased to be a member of a new coalition of more than 200 consumer, civic, labor, and civil rights organizations – Americans for Financial Reform – that is working to cultivate integrity and accountability within the US financial system. I serve on the executive committee of that coalition.

Despite recent talk of recovery, the U.S. economy remains mired in the worst economic crisis in more than half a century. And while it appears we have avoided a second Great Depression, today's economy has earned the status of the "Great Recession." The pace of deterioration of the economy has moderated and we are no longer in free fall. A growing number of economists are looking forward to modest growth in GDP in the third quarter of this year.

Yet, despite the early positive signs of a turnaround in the economy, even the most optimistic economists are expecting a "jobless recovery." That phrase is an acknowledgement that unemployment will likely remain high throughout 2010 in spite of positive GDP numbers. In fact, the Open Market Committee of the Federal Reserve estimates that the unemployment is unlikely to return to pre-recession levels in the next six years.[1]

For most people, a "jobless recovery" is not a recovery at all. Rising GDP, without job growth, is a meaningless statistic in the real world where families are struggling to pay the mortgage, buy food, afford decent health care, pay college tuition for their children, or save to ensure they can

[1] Minutes of the Federal Open Market Committee, April 28-29, 2009. Federal Reserve Board. Published May 20, 2009. Accessed online at http://www.federalreserve.gov/monetarypolicy/fomcminutes20090429.htm.

retire in dignity. Mark Vitner, a senior economist at Wells Fargo, sums it up this way: "It's going to be a recovery only a statistician can love."[2]

Without improving employment, sluggish growth will likely linger for some time. Consumer spending, for example, which accounts for more than 70 percent of all economic activity, will not recover until consumers stop fearing they could lose their homes, their jobs, or both. A *Bloomberg News* survey of economists found that consumer spending is not expected to grow at a rate of more than 2percent per year until sometime in 2011. This July, consumer credit fell at a 10 percent annualized rate, which was five times greater than the drop anticipated by economists. [3] As Ryan Sweet, an economist for Moody's Economy.com sees it, "consumers… won't be leading us out of this recession."[4]

Consumers are in no position to stage a comeback. Poverty figures released just over a week ago by the Census Bureau highlight the tenuous position in which American households find themselves. From 2007 to 2008 the poverty rate rose from 12.5 percent to 13.2 percent. The additional 2.6 million Americans who fell into poverty last year brings the total to 39.8 million people.[5] Median income also sank to the lowest level in more than ten years. As Harvard University economics professor Lawrence Katz put it, "We've basically seen a lost decade."[6]

Experts anticipate that these dismal statistics will only get worse in 2009. Consider that the total number of jobs lost in the first six months of 2008 was 291,000, while the total number of jobs lost in the first six months of 2009 was more than ten times greater, at 3.3 million. Furthermore, as of July, the National Employment Law Project anticipated that 1.5 million Americans will

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[2] Shin, Annys. "A Recovery Only a Statistician Can Love." *Washington Post*. August 12, 2009. Accessed September 4, 2009 at http://www.washingtonpost.com/wp-dyn/content/article/2009/08/11/AR2009081100988.html?hpid=topnews.
[3] Willis, Bob and Vincent Del Giudice. "Record Plunge in U.S. Consumer Debt Signals Weakened Spending." *Bloomberg News*. September 9, 2009. Accessed online at http://www.bloomberg.com/apps/news?pid=20601087&sid=avvF5aNtrCfc#.
[4] Furthermore, consumer borrowing decreased by a record $26.1 billion. See: Willis, Bob and Vincent Del Giudice.
[5] Morello, Carol and Dan Keating. "Millions More Thrust Into Poverty." *Washington Post*. September 11, 2009.
[6] Morello, Carol and Dan Keating.

exhaust their unemployment benefits by the end of 2009,[7] including 400,000 at the end of September alone.[8] Persistent long-term unemployment and the possibility that millions will exhaust benefits and have little to nothing on which to fall back has led the House of Representatives to consider a bill to extend benefits to 79 weeks in states with unemployment above 8.5 percent.[9] Due to the increases in long-term unemployment and the accelerated pace of job losses, analysts anticipate that the 2009 poverty figures will be far larger.[10]

The financial services sector remains in a precarious state despite recent positive earnings news. In fact, a close examination of the fine print and footnotes to the positive earnings reports of many large financial firms reveals that creative accounting, massive federal subsidies, and one-time asset sales have replaced innovative finance as primary sources of profits for many firms within the financial services industry.

Lending by large banks continues to fall despite improved earnings reports. The total amount of loans held by the 15 largest banks decreased by nearly 3 percent in the second quarter of this year,[11] and more than half of the loan volume in April and May came from refinancing mortgages and renewing credit to businesses—not issuing new loans—according to an analysis by the *Wall Street Journal*.

In fact, according to FDIC records, more than 28 percent of banks were unprofitable in the second quarter of 2009—an all-time second quarter record. [12] At the current pace of bank

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[7] Delaney, Arthur. "1.5 Million to Exhaust Unemployment Benefits by the End of the Year." *The Huffington Post*. July 17, 2009. Accessed September 4, 2009 at http://www.huffingtonpost.com/2009/07/17/15-million-to-exhaust-une_n_238281.html.

[8] Luhbi, Tammi. "Unemployment Benefits: Bill Could Help More than 1 Million Jobless." *CNN Money*. September 22, 2009. Accessed online at: http://money.cnn.com/2009/09/22/news/economy/extending_unemployment_benefits/?postversion=2009092205.

[9] Luhbi, Tammie. "Unemployment Benefits: Bill Could Help More than 1 Million Jobless."

[10] Homan, Timothy and Mike Dorning. "U.S. Poverty Rate Rises, Median Income Falls." *Bloomberg News*. September 10, 2009.

[11] Enrich, David and Dan Fitzpatrick. "Loans Shrink as Fears Linger." *Wall Street Journal*. July 27, 2009. Accessed September 4, 2009 at http://online.wsj.com/article/SB124865259057482435.html.

[12] Data is tracked and records are set by the quarter in order to account for seasonal adjustments in bank incomes. Nasripour, Shahirien. "Percent of Money-Losing Banks Set An All-Time High in Second Quarter." *Huffington Post*. August 31, 2009.

failures, this year will greatly exceed those of 2008, which was the worst year in the industry's history.

And while non-financial businesses are generally slowing their pace of contraction or even growing again, much of the improved earnings are the result of increased productivity achieved in part through payroll reductions. Moreover, many corporations that reported profits so far in 2009 are multinational firms that are finding profitable markets overseas and creating jobs outside of the United States. In short, they are succeeding in spite of—not because of—the health of the U.S. economy.

The Foreclosure Crisis Continues

Perhaps the most interesting aspect of the economic data pointing to a modest recovery is that it ignores the fact that foreclosures—the problem that imploded the financial markets and economy in the first place—continue to rise.

Already this year, more than 1.5 million families experienced foreclosure in the first six months of the year and at least another 1.5 million foreclosures are expected to occur by the end of 2009.[13] Just in the month of August, a total of 358,471 properties went into default or foreclosure, according to RealtyTrac, Inc. That was the sixth month in a row that new foreclosure filings surpassed 300,000.[14] Although the pace of new foreclosures slowed between July and August, this rate is up 18 percent year-over-year,[15] and the Mortgage Bankers Association reports that the national delinquency rate is at an all-time high.[16] With 9.24percent of borrowers behind in payments by at least thirty days, the foreclosure crisis is nowhere near its end.

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[13] Schreiner, Bruce. "Last minute Negotiations Ease Some Foreclosures." *Associated Press.* August 21, 2009. Accessed September 4, 2009 at http://www.google.com/hostednews/ap/article/ALeqM5gTeK2ymeqJh-G5ewsuKgk9AnktOQD9A7EI080.

[14] Taub, Daniel. "U.S. Foreclosure Filings Top 300,000 for Sixth Straight Month." *Bloomberg News*. September 10, 2009.

[15] Pisani, Joseph. "Foreclosures Up From Last Year; Remain Near Record Levels." *CNBC*. September 10, 2009. Accessed online at: http://www.cnbc.com/id/32766035.

[16] Wasik, John. "Housing's 'Poverty Effect' Fouls Up Recovery." *Bloomberg News*. September 2, 2009.

Foreclosures continue to grow as the nature of the crisis has evolved. The first wave of foreclosures was driven by reckless loan products, but the crisis is now fueled by unemployment and loss of income. In 2009, nearly 60 percent foreclosures are triggered by unemployment.[17] Other factors that are contributing to the foreclosure crisis include inadequate loan modifications and the coming wave of resets on the second generation of risky loan products.

Research by Professor Alan White of Valparaiso University shows that loan servicers are failing to modify significant numbers of loans to achieve long-term sustainability. In recent testimony before Congress, Professor White notes that in June 2009, three months into the government's Making Home Affordable program, there were roughly ten times as many liquidated foreclosure sales as there were loan modifications with debt reduction.[18] Yet, debt reduction is the more important characteristic of a sustainable loan modification.

Professor White finds that the most common voluntary loan modification involves adding unpaid interest and fees to the balance, so that the homeowner owes more, rather than less, after the modification. While about 60percent homeowners who receive loan modifications through the Home Affordable Modification Program achieve reduced mortgage payments, many of these modified loans will revert to the original terms in three to five years. While these types of modifications may allow homeowners and lenders to avoid foreclosures now, over the long term, "homeowners will have no incentive to continue struggling to make payments."[19]

Moreover, lenders are studiously ignoring the next wave of foreclosures looming on the horizon. From 2004 to 2007, pay-option adjustable rate mortgages, known as option ARMs, totaled $750 billion of lending activity.[20] Refinancing has reduced the amount of outstanding option ARMS to

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[17] "Not Out of the Woods: A Report on the Jobless Recovery Underway." The New America Foundation. June 14, 2009. Accessed online at http://www.newamerica.net/files/TheJoblessRecoveryJune2009.pdf.
[18] White, Alan. "Testimony on Home Foreclosures: Will Voluntary Mortgage Modification Help Families Save Their Homes?" Submitted to the U.S. House of Representatives, Committee on Financial Services, Subcommittee on Commercial and Administrative Law. July 9, 2009.
[19] White, Alan.
[20] Leland, John. "Loans that Looked Easy Pose Threat to Recovery." *New York Times*. August 28, 2009. Accessed September 4, 2009 at http://www.nytimes.com/2009/08/27/us/27arms.html?_r=1&ref=business.

$189 billion, about 70 percent of which will reset by 2011.[21] The average reset of option ARMS will increase monthly payments by an average of $1,053—and these loans were so poorly underwritten that many have already failed before the introductory periods end.[22] In total, there are roughly 2.8 million outstanding interest-only mortgage loans valued at $908 billion, which will reset to fully amortizing loans over the next few years.[23]

The net impact, according to the Center for Responsible Lending, is that as many as 12 million homes will be lost to foreclosure by the end of 2012.[24]

It is difficult to understand how a meaningful recovery can develop without first more aggressively addressing the foreclosure crisis.

Not an Equal Opportunity Economic Crisis

The current crisis is having a disproportionately negative impact on communities of color in two ways. First, communities of color are experiencing higher levels of foreclosures than their non-Hispanic white counterparts, and second, they are more negatively impacted by rising unemployment. Since the recession began in December 2007, more than 6.9 million jobs have been eliminated, bringing the national unemployment rate to 9.7 percent in August of 2009.[25] The rate of job loss for African Americans is now more than 15 percent, and for Latinos it is 13 percent.[26] The black unemployment rate had not fully recovered from the 2001 recession before the start of the current economic downturn. Unemployment for American Indians living on reservations is at 22 percent, scarcely lower than the Depression-era national unemployment rate

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[21] ElBoghdady, Dina. "Another Wave of Foreclosures Looms." *Washington Post*. September 9, 2009. Accessed online at http://www.washingtonpost.com/wp-dyn/content/article/2009/09/08/AR2009090803507.html.
[22] ElBoghdady, Dina. "Another Wave of Foreclosures Looms."
[23] Streitfeld, David. "Interest-only Loans Start to Backfire." *New York Times*. September 8, 2009. Accessed online at http://www.nytimes.com/2009/09/09/business/09loans.html?ref=business.
[24] McGraine, Victoria. "White House's $50 Billion Foreclosure Plan a Bust So Far." *Politico*, July 17, 2009.
[25] Homan, Timothy. "Job Losses in U.S. Slow as Unemployment Hits 26-year High." *Bloomberg News*. September 5, 2009. Accessed online at http://www.bloomberg.com/apps/news?pid=20601087&sid=aVmZJLQoKv2g.
[26] "The Employment Situation—August 2009." Bureau of Labor Statistics, U.S. Department of Labor. September 4, 2009. Accessed online at http://www.bls.gov/bls/newsrels.htm#OEUS.

of 25 percent.[27] Furthermore, while the national poverty rate is 13.2 percent, the African-American poverty rate is 24.7 percent, the Hispanic poverty rate is 23.2 percent.[28]

Thus, the Kirwan Institute at Ohio State University has concluded that "people of color have been in a recession for five years and have entered a depression during the current economic crisis."[29] The overrepresentation of minorities in unemployment has compounding long-term effects on wealth; many households never fully catch up from the financial impacts of the current wave of unemployment. A recent study reported in *The New York Times* indicates that it can take as long as twenty years for workers laid off during a recession to overcome earnings losses.[30]

Because African Americans and Latinos have comparatively few savings, they are poorly positioned to survive long-term unemployment. In fact, for every dollar of net worth held by non-Hispanic white Americans, African Americans hold ten cents, and Latinos hold slightly less than five cents. Home equity represents a much larger share of net worth for African Americans and Latinos. When housing wealth is omitted from the comparison, for every dollar that non-Hispanic whites hold, African Americans hold only a penny and Latinos hold less than one cent.[31] Because African Americans and Latinos have so few resources on which to fall back in a crisis, potentially millions of minority households could find themselves falling out of the middle class and into poverty by the time the economy recovers. United for a Fair Economy, a Boston-based policy group, estimates that African Americans could experience the greatest loss of wealth since Reconstruction, with more than 33 percent of African-American households and 41 percent of Latino households at risk of falling out of the middle class and into poverty.[32]

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[27] Johnson Pata, Jacqueline. "Testimony on the Subject of the Silent Depression: How are Minorities Faring in the Economic Downturn." Presented to the U.S. House of Representatives, Committee on Oversight and Government Reform. September 23, 2009.
[28] "Income, Poverty, and Health Insurance Coverage in the United States: 2008."
[29] "Preliminary Report of the Impact of the Economic Stimulus Plan on Communities of Color." Kirwan Institute for the Study of Race and Ethnicity. February 25, 2009.
[30] Luo, Michael. "Income Loss Persists Long After Layoffs." *New York Times*. August 4, 2009. Accessed September 4, 2009 at http://www.nytimes.com/2009/08/04/us/04layoffs.html?hp.
[31] Wolff, Edward. "Recent Trends in Household Wealth in the U.S.: Rising Debt and the Middle Class Squeeze." Levy Economics Institute of Bard College. 2007. Accessed online at: http://www.levy.org/pubs/wp_502.pdf.
[32] Rivera, Amaad, Jeannette Huezo, Christina Kasica, and Dedrick Muhammad.

Add to that reality the impact of the foreclosure crisis on African Americans. More than half of all home loans made to African Americans in recent years were high-cost, subprime loans associated with the most deceptive and irresponsible lending behavior. Those loans also represent a disproportionately large fraction of the loans that failed in the first wave of the foreclosure crisis.[33] African Americans have already experienced a full three-percentage point drop in their homeownership rate since 2004.[34]

The community and family impacts of foreclosure

When an individual or family loses a home to foreclosure, the effects are devastating beyond the financial loss to that household. A study published recently by the Urban Institute documents multiple negative impacts resulting from foreclosure. The challenge of finding a new place to live, for example, can be particularly difficult. The study notes, for example, that most people displaced by foreclosure move in with family and friends. Many others go to emergency shelters or find themselves on the streets. Because foreclosure causes a person's credit rating to plummet, it can be difficult to rent an apartment even if the prospective tenant has the requisite income and security deposit.[35]

Foreclosure has a particularly harmful effect on children. If a family loses its home to foreclosure and cannot find a suitable apartment in their neighborhood, children may be forced to leave their schools, social networks, and familiar community surroundings, all of which can hinder their educational performance and long-term socioeconomic wellbeing. Families experiencing foreclosure may also face serious blows to the mental and emotional health of both adults and children. The stress and confusion of the situation can affect people physically as they are less

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[33] Rivera, Amad, Jeannette Huezo, Christina Kasica, and Dedrick Muhammad. "Silent Depression: State of the Dream 2009." United for a Fair Economy. January 15, 2009. Accessed online at http://www.faireconomy.org/files/pdf/state_of_dream_2009.pdf.

[34] African-American homeownership peaked at 49.1percent in 2004 and declined to 46.1percent as of 2007. Source: U.S. Census Bureau. Housing Vacancies and Homeownership Annual Statistics 2007. Table 20: Homeownership by Race and Ethnicity of Householder. Accessed online at http://www.census.gov/hhes/www/housing/hvs/annual07/ann07ind.html.

[35] Kingsley, Thomas, Robin Smith, and David "The Impacts of Foreclosure of Families and Communities." The Urban Institute. July 1, 2009. Accessed online at: http://www.urban.org/UploadedPDF/411910_impact_of_foreclosures_primer.pdf.

able to attend to their health. Elderly Americans face especially daunting challenges as they seek to overcome foreclosure. Studies show that they are especially vulnerable to physical and emotional difficulties when they experience forced relocation. Seniors also have limited time and income to recover.

Given that foreclosures are disproportionately occurring in minority communities, the long-term effects of the foreclosure crisis on African-American and Latino neighborhoods and families is not only destroying African-American and Latino wealth, it is also creating conditions that will further limit their abilities to accumulate assets and achieve upward economic mobility.

America's History of Discrimination

Current wealth disparities are not a result of market forces or the invisible hand of Adam Smith. Rather, they are the consequence of the visible hand of discrimination and its legacy. America has a long and complex history of discrimination, much of which continued a full century after slavery was abolished.

Starting in 1896 with the Supreme Court's decision in *Plessy v. Ferguson*, which established the "separate but equal" doctrine, public policy was crafted with the intent to isolate black communities and deny those communities access to credit and services. This continued during the New Deal with the Home Owner's Loan Corporation (HOLC), which was established to help homeowners facing foreclosure. HOLC explicitly refused to approve loans in African-American communities and institutionalized the practice of redlining.[36]

After World War II, discrimination against African Americans continued with the Federal Housing Act and the G. I. Bill. Although these programs were enacted to make homeownership affordable for the majority of American families, including returning veterans, they purposefully reinforced residential segregation through their lending practices. As isolated minority

[36] For further information, see: Carr, James H. "Testimony on the Subject of Fair Housing and Equal Oppportunity." Presented to the National Commission on Fair Housing and Equal Opportunity. Atlanta, Georgia. October 17, 2008. See also: Carr, James H. and Nandinee K. Kutty, Eds. *Segregation: The Rising Costs for America*. Routledge: New York, 2008.

communities struggled to thrive in the face of redlining and lack of basic services, they became targets of government deconstruction programs. The Urban Renewal program, for example, literally bulldozed entire neighborhoods of working-class African Americans. Entire struggling communities were leveled and residents moved into bleak concrete towers that were unfit for human habitation.

These policies achieved their goal of encouraging the segregation and marginalization of black communities. The importance of this history of discriminatory government policy cannot be understated. The challenges that minority communities face today in terms of housing, employment, and wealth accumulation are a direct result of the compounding and cumulative effects of discriminatory policies and institutionalized barriers to opportunity.

Predatory Lending

Predatory lending, the explicit peddling of high-cost loans to vulnerable communities through deception and coercion, is only the most recent manifestation of continuing discrimination against communities of color in the financial markets.

In the wake of the collapse of the subprime mortgage market, many critics have blamed laws that were enacted to ensure that minority communities are no longer discriminated against in the housing market or denied access to fair, responsible credit. They charge that the Community Reinvestment Act (CRA), a law that requires banks to meet the credit needs of the communities they serve, forced lenders to make bad home loans to unqualified low-income consumers. They also defend lenders' abusive and predatory behaviors, saying that lenders were pressured by policymakers to increase homeownership by minorities who could not legitimately afford to own. Neither argument is based in fact or logic. According to the Federal Reserve Board, only 6 percent of high-cost subprime loans to low- and moderate-income households originated by

banks were subject to CRA regulation.[37] The vast majority of reckless, irresponsible lending was carried out without regard to CRA.

The growth in origination of predatory, high-cost loans had little to do with legitimate financial qualifications of the borrowers. A 2008 study by the *Wall Street Journal* found that more than 60 percent of borrowers with high-cost subprime loans had credit scores sufficient for them to have qualified for a prime market home loan. The Center for Responsible Lending released an analysis of loan outcomes that controlled for income and credit history, and found that minorities were significantly more likely than whites to receive high-cost loans.[38] Moreover, racial disparities in lending increase as the income level of borrowers increases.[39]

The disproportionate issuance of high-cost loans to minorities also had nothing to do with lenders attempting to increase homeownership rates among minority families. According to the Center for Responsible Lending, less than 10 percent of subprime loans originated between 1998 and 2006 were for first time homeownership.

In reality, the subprime mortgage market collapsed because regulation of the mortgage markets and financial services sector was largely absent and, where it did exist, inadequate. This lack of oversight allowed deceptive, reckless, and irresponsible predatory lending to grow unchecked. This crisis percolated for years until it boiled over and overwhelmed not just the mortgage markets, but the entire financial system.

Almost every institutional actor in the home mortgage financing process played a role in the collapse. Brokers steered borrowers into risky high-cost loans regardless of their incomes or

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[37] Krozner, Robert. "The Community Reinvestment Act and the Recent Mortgage Crisis." *Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act*. Joint publication of the Federal Reserve Banks of Boston and San Francisco. February 2009.
[38] Boccian, D., K. Ernst, and Wei Li. "Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages." Center for Responsible Lending. 2006.
[39] "Income is No Shield in Lending, III." Joint publication of National Council of Negro Women and National Community Reinvestment Coalition. June 2009. Accessed online at: http://www.ncrc.org/images/stories/pdf/research/ncrc%20nosheild%20june%2009.pdf.
See also: "Race and Recession: How Inequity Rigged the Economy and How to Change the Rules." Applied Research Center. May 2009. Accessed online at http://arc.org/downloads/2009_race_recession.pdf.

credit scores. They were allowed to collect kickbacks in the form of yield spread premiums if they could mislead borrowers to accept loans offered at higher than required interest rates. Lenders offered high-risk products (such as the well-known exploding 2/28 and 3/27 mortgages) that required refinancing within the first two-to-three years in order to remain affordable to borrowers. They pursued inadequate and irresponsible underwriting standards that included excessive levels of low- or no-documentation loans, failure to establish escrow accounts for taxes and insurance, prepayment penalties, and the use of second liens in lieu of down payments.

Appraisers inflated home valuations, driving prices to unsustainable record highs. Credit ratings agencies indiscriminately stamped "investment grade" on securities backed by subprime bonds regardless of their actual risk level. Investment banks paid premium prices for those high-risk loans without regard for the real value of the mortgages that backed those bonds. In the end, the entire system was converted into a massive Ponzi scheme that collapsed almost immediately as home prices began to soften in 2006.

Rebuild, Not Stabilize, Communities

In order to build healthy, sustainable, thriving communities, and ensure that all Americans are able to benefit from economic recovery, five specific issues must be addressed.

First, ending the foreclosure crisis is a critical challenge.

Second, restructure financial regulation with an emphasis on consumer protection.

Third, implement innovative programming to stimulate growth in communities that have been hardest hit.

Fourth, create a national housing policy.

Fifth, improve enforcement of the Fair Housing Act.

1. Stem the Rising Tide of Foreclosures

The Obama Administration's "Making Home Affordable" (MHA) is the most comprehensive government plan to address the foreclosure crisis. It aims to provide relief to 3 to 4 million homeowners over several years through a combination of mortgage refinancing and modification. But the program is off to a slow start for a variety of program design and implementation challenges. The best estimates to date are that 360,000 homeowners have received loan modifications since the program was launched six months ago.[40] That is only 12percent of all homeowners who are eligible.[41]

The Administration has been aggressive about responding to program weaknesses and tightening guidelines to improve performance. But the program continues to struggle due largely to an intransigent servicing industry whose financial interests not aligned with investors or the public interest.

Servicer Intransigence

Professor Alan White notes that within the pool of subprime and alt-A mortgages that he tracks, "the foreclosure losses on each mortgage were about ten times the amounts of the write-offs on modifications." Specifically, data for June 2009 shows that the average loss on a liquidated foreclosure is $143,987, while the average write-off on loan modifications is only $14,353.[42] In short, although it is far more financially advantageous for lenders to deliver long-term sustainable loan modifications,[43] they continue to disregard the severity of the foreclosure crisis that has destroyed more than $7 trillion in housing equity.[44]

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[40] Taub, Daniel. "U.S. Foreclosure Filings Top 300,000 for Sixth Straight Month." *Bloomberg News*. September 10, 2009.
[41] Luhby, Tami. "12percent of Eligible Borrowers Helped by Obama Plan." *CNN Money*. September 9, 2009. Accessed online at http://money.cnn.com/2009/09/09/news/economy/Obama_foreclosure_rescue/?postversion=2009090912.
[42] White, Alan.
[43] Bank capital could be impared in the instances where modifications involve discounts far exceeding current write-downs on mortgage loans.
[44] Willis, Bob and Vincent Del Giudice.

Loan servicers also remain unresponsive to the needs of the American public, even though there are significant subsidies available to them under the Administration's Home Affordable Modification Program. A major problem with Making Home Affordable is that while it offers plenty of carrots, it has no meaningful sticks to compel more responsible actions by servicers.

In Congressional testimony this month before the House Committee on Financial Services, Alys Cohen of the National Consumer Law Center detailed how problems and inconsistencies in servicers' implementation of HAMP have hurt homeowners in need of loan modifications.[45] She documents that many servicers remain understaffed and much of the existing staff is undertrained and unable to provide the necessary level of support. Cohen finds that homeowners and housing counselors report waiting for several months after submitting applications, only to be given a prohibitively short time frame to submit further documentation.

According to Cohen, in addition to the "alarming ignorance of HAMP" displayed by many servicers, others are violating the program's basic requirements. Many servicers, for instance, charge fees to homeowners who receive modifications, while other participating servicers refuse to offer HAMP modifications to some homeowners, and many servicers are continuing to initiate foreclosures and sell homes at foreclosure sales while HAMP reviews are in progress, in direct violation of HAMP regulations.[46]

Cohen's findings on the widespread non-compliance by servicers participating in Making Home Affordable are repeated in an August 2009 report by the *Associated Press*. The *AP* analysis found that 30 of the 38 servicers it studied have been sued by homeowners and fair housing advocates for legal violations and failure to comply with MHA rules and regulations.[47]

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[45] Cohen, Alys. "Testimony on the Subject of Progress on the Making Home Affordable Program: What are the Outcomes for Homeowners and What are the Obstacles to Success?" Presented to the U.S. House of Representatives, Committee on Financial Services, Subcommittee on Housing and Community Opportunity. September 9, 2009.
[46] Cohen, Alys.
[47] Wagner, Daniel. "Mortgage Servicers Accused of Harassing Borrowers, Illegal Fees." *Huffington Post*. August 5, 2009. Accessed September 4, 2009 at http://www.huffingtonpost.com/2009/08/05/mortgage-servicers-accuse_n_252081.html.

In her testimony, Cohen presented the National Consumer Law Center's recommendations to improve HAMP. Highest on her list of priorities is increased transparency, including making public the model for determining a home's Net Present Value. Mechanisms for enforcement and compliance, such as providing an independent review process to homeowners who are denied HAMP modifications and the establishment of an ombudsman to hear and address complaints about the process and specific servicers' actions. Cohen also makes clear that HAMP must provide principal reductions, not forbearance, if it is to provide meaningful, sustainable relief.[48]

Even under the best circumstances, however, Making Home Affordable has significant limitations. Cohen estimates that at best, HAMP could address only one third of the foreclosure crisis.

Solutions

The bottom line: A more robust response to the foreclosure crisis is needed. A new version of the Great Depression-era Homeowners Loan Corporation (HOLC) is warranted. The new entity would more aggressively pursue loan modifications using exceptional powers, such as eminent domain, to secure toxic loan products from investors and modify as many loans as possible to make them affordable and sustainable.[49] NCRC first proposed such an entity in January 2008 in testimony before the U.S. House of Representatives Committee on the Judiciary, Subcommittee on Commercial and Administrative Law.[50] Under the NCRC proposal, loans would be purchased at a reasonable discount (between current market value and face value). Discounts secured through the purchase process would be applied to modify the loans, including principal

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[48] Cohen, Alys.
[49] For more detail see: Carr, James H. "Responding to the Foreclosure Crisis." *Housing Policy Debate*, Vol. 18, Issue 4. 2007. Pages 837-860.
[50] Carr, James. "Testimony on the subject of Responding to the Foreclosure Crisis." U.S. House of Representatives, Committee on the Judiciary, Subcommittee on Commercial and Administrative Law. January 29, 2008. Accessed online at: http://www.ncrc.org/images/stories/mediaCenter_testimony/respondingpercent20topercent20thepercent20foreclosurepercent20crisis.pdf.

forgiveness. This process would greatly reduce the cost to taxpayers of broad-scale loan modification.

A new HOLC could also be used to address the multiple problems created by unemployment-driven foreclosures. This could include tying foreclosure moratoria to unemployment benefits. In instances where foreclosure is imminent, families could be allowed to remain in their homes with rental agreements in order to avoid further stress and disruption for families and additional vacant and abandoned properties that exacerbate declining home prices.

More homeowners could be given access to funding for emergency grants and/or loans that allow them to continue paying their mortgage while they are unemployed.[51] This measure could provide a safety net for the one out of every six American workers who are unemployed, "partly employed, [or] who have given up on hunting for jobs because there are so few jobs to be had,"[52] many of whom are or soon will be at risk of foreclosure.

Reform of the bankruptcy code is also warranted. It was proposed as part of the President's Making Home Affordable Program but defeated by Congress. Similar legislation should be reintroduced and passed into law. Currently, bankruptcy courts can modify repayment terms on the outstanding debt on a luxury yacht or investment property, but not the family home. This disparity in treatment is unfair, inequitable, and serves no public policy goal. Furthermore, expanded bankruptcy protection could address as much as 30 percent of loans heading to foreclosure and at no cost to the American taxpayer. The prospect of repayment terms being determined in bankruptcy court would also encourage more servicers to preclude homeowners' access bankruptcy relief.

2. Refocus Financial System Regulation on the Interests of Consumers

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[51] Pennsylvania's Home Emergency Mortgage Assistance Program, for example, provides a two-year loan of up to $60,000 for homeowners who become involuntarily unemployed to use for mortgage payments. For more information, visit the program website: http://www.phfa.org/consumers/homeowners/hemap.aspx

[52] Meyerson, Harold. "Unhappy Labor Day." *The Washington Post*, September 7, 2009. Accessed September 16, 2009. http://www.washingtonpost.com/wp-dyn/content/article/2009/09/06/AR2009090601194.html.

Nobel prize-winning economist Joseph Stiglitz sums up the financial crisis this way: "our financial system discovered there was money at the bottom of the [wealth] pyramid and made a concerted effort to make sure the money did not remain there."[53] For more than a decade, financial institutions have increasingly engaged in practices intended to mislead, confuse, and otherwise limit a consumer's ability to judge the value of financial products offered in the market and make informed decisions. Stated otherwise, for many financial firms, deception became the operative business model.

Elizabeth Warren, a Professor of Law at Harvard University and Chair of the Congressional Oversight Panel on the Troubled Asset Relief Program, has developed a detailed list of the "tricks and traps" that financial institutions use to make unsafe financial products appear attractive to consumers. She also adds that these financial institutions build unjustified and unethical fees and penalties into the terms and conditions of such products to turn a profit at the expense of trusting borrowers.

Only a few years ago, for example, the typical terms and conditions statement for a credit card was only a single page. Today, terms and conditions sheets are steeped in complex legal jargon and can number up to 30 pages. Warren asserts that this is an unjustifiable burden on the average consumer, and is in fact so onerous that she herself has difficulty understanding them. Says Warren: "I teach contract law at Harvard Law School and I can't understand my credit card contract."[54]

In response to deceptive business practices, Congress has had to go so far as to mandate that at a minimum, contracts should be printed "in not less than twelve-point type,"[55] because in addition to the complex and confusing legal terminology, credit card companies were printing their required disclosures to consumers with such small print it could barely be read by the human eye. The "tricks and traps" used to market high-cost, unsustainable home loans greatly

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[53] Stiglitz, Joseph. "Testimony on Too Big To Fail or Too Big to Save? Examining the Systemic Threats of Large Financial Institutions." Presented to the U.S. House of Representatives Joint Economic Committee. April 21, 2009.
[54] Warren, Elizabeth. Televised interview, *NOW on PBS*. January 2, 2009. Transcript available at: http://www.pbs.org/now/shows/501/credit-traps.html.
[55] Sec. 14 (d)(1) " Credit Card Holders Bill of Rights Act of 2009." H.R. 627. 111th Congress, First Session. 2009. Available online at: http://thomas.loc.gov/cgi-bin/query/C?c111:./temp/~c111W5U0s9.

complicated, if not impaired, the ability of a consumer to make an informed decision about the most appropriate mortgage product for his or her individual needs and financial circumstances.

Eliminating these "tricks and traps" requires a multi-pronged response including: (1) enacting a consumer financial protection agency with broad power over the nation's consumer financial protection laws; (2) enacting a strong national anti-predatory mortgage lending law; and (3) modernizing the Community Reinvestment Act to encourage and ensure access to safe and sound lending equitably across communities.

The Role of Consumer Protection in the Financial System

The Obama Administration has proposed the establishment of a Consumer Financial Protection Agency[56] that would consolidate the highly fragmented system of consumer financial protection laws currently enforced by six separate agencies. That new agency would have broad authority to oversee products like home mortgages and credit cards, and services including real estate appraisals, tax preparation, and debt collection. It would promote clear and understandable terms in contracts, and fair, safe, and reliable financial products and services.

The proposed CFPA would not be susceptible to the same regulatory arbitrage that has characterized the current regulatory regime. Regulatory arbitrage allowed financial firms to select their regulator. The regulator offer the most lax consumer protection was the favored regulatory institution. This reality fueled a race to the bottom for consumer protection that eventually imploded the financial system. Competition is an essential element of a free market, but oversight and enforcement of the law is not, nor should it be, available for purchase in a free market.

Opponents of a consumer financial protection agency have argued that such an agency would undermine the safety and soundness of the financial system. Yet, the safety and soundness of the financial system begins with and relies heavily on the safety and soundness of the products

[56] Section 3. "Financial Regulatory Reform: A New Foundation." U.S. Department of the Treasury. June 2009. Accessed online at: http://www.financialstability.gov/docs/regs/FinalReport_web.pdf.

offered to the public. If the extension of credit by a financial firm promotes the economic wellbeing and financial security of the consumer, the system is at reduced risk of failure. If, however, financial products exploit consumers – even if they are highly profitable – the financial system is in jeopardy.

Arguments against the creation of a CFPA also include the notion that product innovation would be stifled and that consumers would lack access to financial services that meet their unique consumer needs. These propositions are without merit, as NCRC President and CEO John Taylor made clear in testimony before the House Financial Services Committee last week.[57] The CFPA, as conceived by the President, would provide consumers with relevant and understandable information that will enable them to make better financial decisions in their best interests.

Some critics speak about standard products as if they are anathema to the private market. However, standard products were the hallmark of the housing industry prior to the "product innovations" that imploded the financial system. The 30-year fixed-rate mortgage has been, for decades, the gold standard of mortgage products, and was responsible for America's extraordinarily high rate of sustainable homeownership. It is this mortgage product that allowed homeownership to become the cornerstone of wealth attainment for the typical American household.

In short, sometimes the best "product innovation" is a quality standard product.

Another argument against a proposed CFPA is that it might cost the American taxpayer too much money. However, the current economic crisis demonstrates that a failure to adequately regulate the financial marketplace will result in far higher costs than managing an agency. To date, $13.9 trillion in household wealth has been lost since 2007,[58] and the government has

[57] Taylor, John. "Testimony on Proposals to Enhance the Community Reinvestment Act." Presented to the United States House of Representatives, Committee on Financial Services. September 16, 2009. Accessed online at: http://www.house.gov/apps/list/hearing/financialsvcs_dem/taylor_ncrc.pdf.
[58] Willis, Bob and Vincent Del Giudice.

extended a total of $23.7 trillion in investments, loans, and guarantees to prop up the financial sector. It is not clear how much of that sum taxpayers can expect to recoup.[59]

Recently, the House Financial Services Committee Chairman Barney Frank proposed a similar consumer financial protection agency. That bill, the Consumer Financial Protection Agency Act of 2009 (H.R. 3126), reinforces the President's proposal in many key areas.[60] But unlike the President's proposal, it leaves primary regulation for the Community Reinvestment Act with the Federal Reserve Board. This is a mistake.

The principal argument against transferring CRA enforcement to the proposed CFPA is that the new agency should address the targeting and sales financial products to individuals only. It is argued that expansion of its mission to incorporate financial services at the community level would overwhelm the agency and undermine its effectiveness. This argument ignores the fact that financial services providers have historically and routinely offered products at a community level. Many firms use race as a proxy for financial vulnerability to concentrate their use of high-cost, deceptive and predatory financial products. The excessive concentration of subprime loans in African-American and Latino communities is one example of this phenomenon.

Moreover, geographically targeted predatory lending practices are not limited to the housing market. Payday lenders, check cashers, rent-to-own establishments, title lenders and other alternative financial services institutions also concentrate in communities of color. Until hyper-segregation of communities of color is no longer a common feature of the American residential landscape, lending discrimination by geography will continue. CRA is the single most powerful tool to purge predatory financial practices at a community level.

Limiting the offering of deceptive and high cost products is only half the battle of ensuring adequate and reasonable access to safe and responsible financial products. America has a long history of redlining, or the complete and deliberate failure to meet the legitimate financial

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[59] Kopecki, Dawn. "U.S. Bailout May Cost $23.7 Trillion, TARP Inspector Says." *Bloomberg News*. July 20, 2009.
[60] "Consumer Financial Protection Agency Act of 2009." H.R. 3126. 111th Congress, First Session. Introduced July 8, 2009. Accessed online at: http://thomas.loc.gov/cgi-bin/query/C?c111:./temp/~c111pzNGRY.

services needs of all communities. The absence of competition for mainstream financial services creates the vacuum in which subprime mortgage, payday and other high cost lenders establish themselves. CRA is the most comprehensive law designed to ensure the extension of mainstream financial services in a safe and sound manner to all communities.

Stated otherwise, failure to include CRA enforcement in the CFPA might result in improvements in the design of payday loans, for example, but payday lenders could still disproportionately target their services to minority communities. In that case, the agency's work would do little to ensure that banks affirmatively serve those communities with high quality, mainstream financial products and services.

Finally, similar to other consumer protection laws with similarly dismal track records for enforcement, CRA has suffered from a lack of commitment from its regulators. Leaving CRA under its current regulators will simply guarantee continued failure to protect the rights of consumers under CRA.

Strengthen and Expand CRA

Strengthening and expanding CRA is also essential. According to the Federal Reserve, nearly 10 million households have no relationship with a mainstream financial institution. And, a recent report by the Center for Financial Services Innovation estimates that there are 40 million under-banked households in the United States.[61] In fact, an *Associated Press* analysis of Census Bureau data reveals that only about ten percent of all new full-service bank branches opened between 2003 and 2008 were located in the urban, minority neighborhoods.[62] Those neighborhoods are already the least well-served by bank branches.

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[61] Herrmann, Michael J. "CFSI Underbanked Consumer Study Fact Sheet." Center for Financial Services Innovation. Updated February 2009. Accessed online at: http://www.cfsinnovation.com/underbanked-study-detail.php?article_id=330525.

[62] Frank and Linda Stuart Ball. "Banks Added 10,000 Branches During Boom but Left Inner Cities Behind." *Huffington Post*. August 17, 2009. Accessed on September 4, 2009 at http://www.huffingtonpost.com/2009/08/17/banks-added-10000-branche_n_261267.html.

Despite the large numbers of unbanked households and the failure of depository institutions to address that lack of access, 97 percent of banks pass their CRA exams. Regulation of CRA under CFPA should improve the rating system for CRA so that assessments of the banking industry better reflect the reality of access to viable financial services by the American public.

Finally, CRA should be expanded to cover non-depository institutions as well as banks. Investment banks, for example, were a principal funder of irresponsible subprime loans. Moreover, the loopholes, exceptions and opt-outs that allow current CRA-covered banks to exempt the activities of their affiliate financial institutions on CRA exams must be eliminated. Loopholes and exceptions have allowed CRA-covered banks to exclude their subprime lending activities from CRA review. In a recent op-ed, Elizabeth Warren cited a Center for Public Integrity study that "found that 21 of the 25 largest subprime issuers leading up to the [foreclosure] crisis were financed by large banks."[63]

Finally, even if CRA is strengthened and expanded, failure to relocate it to the new CFPA in order to ensure enforcement of the law would make that legislation a Pyrrhic victory.

3. Rebuild Communities Harmed by the Crisis

The Kirwan Institute at the Ohio State University has performed a comprehensive examination of the potential impact on communities of color of both the economic crisis and the stimulus programs implemented to spur recovery.[64] The most fundamental conclusion of the Kirwan Institute's report is that neither the American Recovery and Reinvestment Act (ARRA) nor the Neighborhood Stabilization Program (NSP) is sufficiently targeted to prioritize funding to protected class communities in a manner that reflects the disproportional damage they are suffering as a result of the current crisis.

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[63] Warren, Elizabeth. "Real Change: Turning Up the Heat on Non-Bank Lenders." *Huffington Post*. September 4, 2009. Accessed online at http://www.huffingtonpost.com/elizabeth-warren/real-change-turning-up-th_b_276887.html.

[64] "Preliminary Report of the Impact of the Economic Stimulus Plan on Communities of Color."

The report recommends crafting recovery implementation policies in a proportional manner that takes into consideration the diverse challenges faced by different segments of the population. In fact, they argue that policies that fail to prioritize the hardest hit communities will likely *increase* inequities. Instead, policies should be "inclusive, yet…target those who are the most marginalized."[65]

Channeling dollars to the individuals and communities that need them most will immediately stimulate the economy and save and create jobs for both the neediest households and the U.S. population generally. Families that live on the edge of survival will pour these recovery dollars immediately back into the economy through spending on groceries, medicine, clothing, child care, energy, transportation, and other basic necessities. That spending would support multiple sectors of the economy and have positive impacts far outside of the communities where dollars are immediately spent.

Prioritizing areas hardest hit by widespread unemployment and mounting foreclosures would also more directly stabilize the housing market and steady falling home prices. Finally, investing in areas most in need of infrastructure improvements would provide a needed enhancement of the quality of life in communities long-neglected. Earlier this year, the Obama Administration has signaled its desire to fund long-neglected infrastructure investments. This would be an important contribution to rebuilding the economy while investing in communities. Dollars appropriated for infrastructure should be linked to and coordinated with other efforts to rebuild communities that have been damaged by the foreclosure crisis.

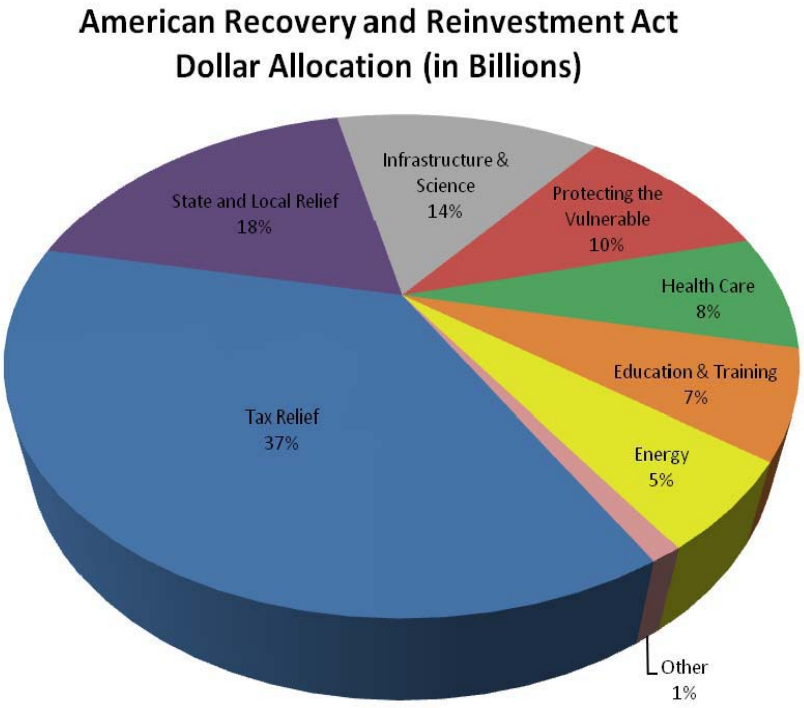
Federal Recovery Efforts: ARRA and NSP

An overall review of the funding priorities in ARRA reveals that, by overall dollar allocation, the largest expenditure category is tax relief, which is a one-time initiative with no long-term impact. Most of the funding for job preservation and creation will not be disbursed until 2010.

[65] "Preliminary Report of the Impact of the Economic Stimulus Plan on Communities of Color."

Furthermore, ARRA has few requirements regarding targeting the communities hardest hit by the foreclosure and unemployment crises. Particularly in comparison to the massive tax relief benefits, the Kirwan Institute argues that some of the most important programs for communities hardest hit by the recession (and facing the worst foreclosure crises) have comparatively modest allocations.[66] The requirement, for example, that only ten percent of rural infrastructure grants be "targeted to persistent poverty counties… with a special priority on areas that have suffered from excessive job loss and foreclosures" is insufficient to overcome the vastly larger barriers to

recovery in communities that have long experienced recession-like conditions and continue to suffer disproportionately.[67]



Source: Preliminary Report of the Impact of the Economic Stimulus Plan on Communities of Color." The Kirwan Institute, February 25, 2009.

[66] "Preliminary Report of the Impact of the Economic Stimulus Plan on Communities of Color."
[67] American Recovery and Reinvestment Act of 2009. H.R. 1. U.S. House of Representatives. January 17, 2009. Available online at: http://www.gpo.gov/fdsys/pkg/PLAW-111publ5/html/PLAW-111publ5.htm.

The Department of Housing and Urban Development's (HUD) Neighborhood Stabilization Program is more targeted than the larger ARRA. NSP attempts to target funding to high-need communities. Its total level of funding under ARRA, however, is too modest to ensure that the hardest-hit communities will receive the funding and investment that they need.

With regard to comprehensive redevelopment, NSP seeks to fund "programs and projects that will revitalize targeted neighborhood(s) and reconnect those targeted neighborhoods with the economy, housing market, and social networks of the community and metropolitan area as a whole." Activities beyond housing stabilization, however, are not eligible for support through NSP grants. In particular, HUD can "not consider requests to allow foreclosure prevention activities."[68] Furthermore, while areas of high vacancy and decline are likely to be disproportionately low-income, there are no direct requirements that targeted neighborhoods must be low-income.

Comprehensive Redevelopment Solutions

America needs a wide-ranging approach to neighborhood redevelopment that is comprehensive and sustainable. Foreclosure prevention, neighborhood stabilization, affordable housing development, and job creation must be linked together as components of a comprehensive redevelopment plan.[69]

Comprehensive redevelopment strategies should simultaneously address housing options for vacant and abandoned properties, identify green building opportunities as a source of job creation, invest in quality infrastructure, and provide community assets such as parks and community gardens. Housing programs should stabilize abandoned properties while implementing strategies to return properties to productive use and rebuild the housing market.

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[68] "Notice of Fund Availability (NOFA) for the Neighborhood Stabilization Program 2 under the American Recovery and Reinvestment Act, 2009." Department of Housing and Urban Development. May 4, 2009.
[69] See the forthcoming work: Carr, James H. "Providing a Context for Community Economic Development." *Community Economic Development: A Legal Guide for Advocates, Lawyers, and Policymakers*. Roger Clay and Susan Jones, Eds. American Bar Association: Washington, 2010.

Funding should prioritize programs that would enhance residents' economic mobility by capitalizing on their existing financial and housing resources, and connect them to mainstream banking services. This crucial step will ensure that existing residents have the tools and ability to participate in and benefit from redevelopment efforts as they enhance their financial assets and gain an ownership stake in redevelopment initiatives.

Funding should also prioritize comprehensive redevelopment plans that include local job requirements in housing market and construction activities. Job requirements should ensure a living wage, offer apprenticeship programs, and include opportunities to advance along a career ladder. Federal programs should allow profits from rebuilding and redevelopment projects to be recycled into job programs and business development.

The cornerstone of community revitalization efforts should be investment in safe, affordable, efficient housing. Two specific housing issues of relevance to community economic development demand attention. First, federal funding should support nonprofits and local governments as they develop and enhance initiatives that identify vacant and abandoned properties, allowing for early intervention and preventive efforts to limit vandalism and crime. Second, communities should prioritize expanding affordable rental housing through ownership of foreclosed properties. Households that have lost their properties and moving to rental units are driving up demand for affordable rental housing.

Adding to the pressure are those families already living in rental housing who find themselves evicted as their landlords allow rental units to go through foreclosure. Federal programs should more aggressively support the ability of community and economic development professionals to work with communities, particularly those with concentrated pockets of foreclosure, to facilitate the transfer of ownership of foreclosed properties into housing trusts or similar vehicles for renovation and return to affordable-housing use.

Another issue is rebuilding the affordable housing market with safe and sustainable loan products. Lease purchase products are promising, particularly in the current environment where the credit scores of potentially millions of consumers have been damaged and savings have been

exhausted. Despite blemished credit histories, millions of household may, nevertheless, be fully prepared to own under reasonable financial circumstances. Lease purchase products might be the way to bring those consumers back into the homeownership market.

Shared-equity mortgages also hold great promise for bringing consumers into the housing market who are unable to make large down payments but are otherwise ready for homeownership. Under a shared-equity arrangement, an investor contributes some or all of the down payment for a home purchase in return for a fixed share of the future home price appreciation. Shared-equity mortgages would also be an important antidote to the market's abuse of financially vulnerable borrowers. Shared-equity mortgages ensure that an investor's equity is on the line and therefore bring the borrower's and investor's interests into alignment. Shared-equity mortgages can enhance affordability by reducing the debt obligation for homebuyers by as much as 20 to 30 percent relative to a no- or very low-down payment product.

Job Creation and the Role of Small Businesses

Recovery dollars for job training programs and job creation should prioritize proposals to create comprehensive training programs. Such training programs should include skills training for jobs in growing industries as well as adult education and GED classes. They should also offer supportive services to overcome common barriers to participation (i.e. transportation, child care), and provide support for formerly incarcerated individuals.

Training and investment dollars should also target green industries and the emerging green economy. There is evidence that jobs created from investment in green projects (such as green infrastructure, energy conservation, renewable energy, and building rehab and reuse) are more likely than non-green jobs to be unionized and to provide benefits and higher wages.[70] Furthermore, green jobs are expected to be a growing sector of the labor market, and it is an area in which nonwhite workers are underrepresented.

[70] Bivens, Josh, John Irons, and Ethan Pollack. "Green Investments and the Labor Market." Economic Policy Institute, April 7, 2009.

Recovery funding for job creation should give priority support to small businesses (those with fewer than 500 employees) because they account for the majority of economic activity in America. In fact, small businesses employ more than half of the American labor force, produce more than half of the country's nonfarm private GDP, make up 99.7 percent of employer firms, and have "created 60percent to 80percent of the nation's net new jobs each year" over the past decade.[71]

Over the past decade, minority-owned enterprises have accounted for more than half of the two million new small businesses in the United States.[72] Despite this recent growth in entrepreneurship, minorities continue to own a disproportionately small number of America's small businesses and a disproportionately small share of profits:

> African Americans make up over 12 percent of our population, but under 6 percent of our businesses and 1 percent of profits; Hispanics are over 13 percent of the population, but only 7 percent of businesses and fewer than 3 percent of profits; and women make up a majority of our population, but account for less than 30 percent of our businesses and just over 10 percent of profits.[73]

The racial disparities in business ownership rates and profits are largely attributable to the fact that minority and women business owners have historically had significantly less access to capital. In the Small Business Association's two largest programs, for example, "the share of dollars of loans to African Americans has been about 5 percent and 2 percent. For women, they've remained about 22 percent;" women and minorities also received "less than 5 percent of the venture capital investments made over the past 40 years."[74]

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[71] Covel, Simona. "Slump Batters Small Business, Threatening Owners' Dreams." Wall Street Journal, December 26, 2008. Accessed September 16, 2009. http://online.wsj.com/article/SB123025114273834377.html
[72] Scott, Betsy. "Making their Mark." The News-Herald, January 11, 2009. Accessed September 16, 2009. http://www.news-herald.com/articles/2009/01/11/news/nh225069.txt
[73] Senator John Kerry. "Statement of Senator John F. Kerry on Business Start-up Hurdles in Underserved Communities: Access to Venture Capital and Entrepreneurship Training." U.S. Senate Committee on Small Business and Entrepreneurship, September 11, 2009. Accessed September 16, 2009. http://sbc.senate.gov/press/record_statement.cfm?id=302832
[74] Senator John Kerry.

During the current economic crisis, small businesses face considerable challenges, including restricted access to credit, diminished consumer spending, and price increases on goods and materials. To support small businesses and promote small business lending, ARRA designated $730 million to the Small Business Administration (SBA) for bridge loans to small businesses and guaranteed backing of loans to small businesses made by private financial institutions.[75] Despite the fact that, according to Senior Advisor to the Secretary of Commerce Rick Wade, minority-owned businesses are suffering disproportionately,[76] neither ARRA nor the SBA's implementation policies require lending to target historically undercapitalized or marginalized business owners.

One alternative to increased targeting of small business loans and job creation funding would be to expanding Community Reinvestment Act (CRA) examination criteria to include the collection of data by race and gender for small business owners. This would encourage lending to minority- and women-owned businesses just as lending to minority and women homebuyers increased when the Home Mortgage Disclosure Act (HMDA) was amended in 1988 to require the reporting of race and gender of the borrower"[77]

In summary, to establish a sustainable recovery plan that benefits all Americans, solutions need to be comprehensive, flexible, dynamic, and targeted. Policies need to address "communities hardest hit by the economic recession and most in danger of falling permanently out of the fabric of American society."[78] To that end, the Center for Social Inclusion recommends that recovery spending be built around the following five principles:

1. Ensure that those most in distress benefit meaningfully

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[75] "SBA's Economic Recovery Efforts and Impact." U.S. Small Business Administration. September 15, 2009. Available online at: http://www.sba.gov/idc/groups/public/documents/sba_homepage/sba_rcvry_aara_imp_factsheet.pdf.
[76] "Minority Businesses Fight to Stay Afloat." National Public Radio, August 25, 2009. Accessed September 16, 2009. http://www.npr.org/templates/story/story.php?storyId=112200627
[77] "Access to Capital and Credit for Small Businesses in Appalachia." National Community Reinvestment Coalition. May 2007.
[78] The Center for Social Inclusion. "Economic Recovery for Everyone: Racial Equity and Propserity." *Poverty and Race*, March/April 2009. 18 (2). Accessed September 18, 2009.

2. Support infrastructure projects that benefit distressed communities, not solidify inequities

3. Address access to credit in communities disproportionately harmed by the collapse of the mortgage market and the job market

4. Recognize differences in labor segmentation by race and gender to ensure an equitable distribution of the stimulus' benefits

5. Provide for data collection on the race, ethnicity, and gender of those served by stimulus money for evaluation purposes[79]

4. Create a National Housing Policy

America has no national housing policy. While successive administrations have had the general goal of increasing homeownership, and some have occasionally expressed the desire to promote mixed-income or supportive-services housing, there are few meaningful national housing goals or objectives against which federal housing programs are measured.

Rather than a defined policy, there is a hodgepodge of programs—many that date back to the Great Depression—which are in need of serious overhaul. The U.S. population has changed dramatically over the past half-century and continues to change rapidly. Moreover, energy and other environmental concerns are now major factors in housing policy considerations. These issues present a host of challenges and opportunities for the nation's housing infrastructure.

Policymakers should have a focused discussion about the goals of housing policy in order to determine how the financial system can better support the achievement of those goals. Questions to be asked include: What is the role of housing policy in promoting vibrant communities and ensuring the economic interests and social wellbeing of the population? And, based on how we answer that question, what are the relationships between housing policy and energy, transportation, education, and other national priorities?

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[79] The Center for Social Inclusion. "Economic Recovery for Everyone: Racial Equity and Propserity." *Poverty and Race*, March/April 2009. 18 (2). Accessed September 18, 2009. http://www.prrac.org/pdf/MarApr2009PRRACstim.pdf

Given the significant housing challenges facing communities of color both before and as a result of the foreclosure crisis, a serious revamp of housing policy is warranted in order to help compensate for the legacy of decades of discriminatory actions and its disproportionately negative repercussions currently undermining minority neighborhoods.

In a 2003 lecture at Harvard University, former HUD Secretary Henry Cisneros suggested that housing should be viewed as an ascending continuum. The lowest step is homeless shelters, moving next to supportive housing, and ultimately to long-term homeownership. Viewing housing as a continuum encourages policymakers to think of households as moving up along a chain of housing successes, rather than approaching housing in a static context. This housing staircase can also be used as a tool to examine federal housing subsidies at each level—to determine where the allocation of public resources might be more effectively and appropriately redirected to channel subsidies to those most in need, and to leverage housing investments to promote upward mobility.[80]

The cost of producing housing is also a critical issue to be addressed in the context of a new national housing policy. Prior to the foreclosure crisis, America was suffering from rapidly growing affordability problems that reached from coast to coast. When the current inventory of unsold homes is off the market and the U.S. economy begins to grow in earnest, those problems may return unless they are effectively addressed now.

The availability of affordable rental housing is a key ingredient of a national housing strategy. Renters need to be able to save money toward a down payment on a mortgage if they are to become homeowners. Yet, half of all renters spend more than 30 percent of their income on housing,[81] and a single minimum wage earner does not make enough money to pay for decent

[80] Cisneros, Henry. "Homes for Americans in the Twenty-First Century: Challenges and Opportunities for the Nation." Fifth Annual Dunlop Lecture, Joint Center for Housing Studies, Harvard University. September 29, 2003. Accessed online at: http://www.jchs.harvard.edu/publications/homeownership/m03-2_cisneros.pdf.
[81] Mishel, Lawrence, Jared Bernstein, and Heidi Shierholz. "The State of Working America, 2008/2009." Economic Policy Institute. Ithaca: Cornell University Press, 2009.

rental housing in any metropolitan area in the nation.[82] These problems will only be exacerbated by record unemployment rates and the foreclosure crisis, as homeowners transitioning to lower cost rental properties will squeeze supply, and 40 percent of all foreclosure evictions have been on rental units.[83]

Another strategy to address affordable housing is to incentivize correcting inefficient land-use patterns. One silver lining of the energy price shock of 2008 was the wake-up call to the American public that our current land-use practices are counterproductive to the public interest. Although energy prices have fallen dramatically from those record highs, they are likely to rebound when the global economy recovers.

As a result, federal policies should tie HOME, Community Development Block Grants (CDBG), and other housing subsidies—along with highway, mass transit, and other infrastructure funds—to communities' sustainable planning and construction practices. This would reduce the need for public subsidies to buy down rents on unnecessarily over-priced housing. Fundamental weaknesses in land-use regulations can also be addressed with programs that encourage greater reliance on new and innovative building technologies; determine the benefits and costs of alternative green technologies; update building codes; and streamline permitting-and-approval processes.

5. Enforce the Fair Housing Act

More than 40 years after the passage of the Fair Housing Act (FHA), the laws protecting the rights of minority families in the housing market remain poorly enforced. Many of today's housing problems result from chronic patterns of discrimination.

Discrimination undermines the economic and social wellbeing of communities and limits access to key opportunities that are essential to upward mobility.

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[82] "Race and Recession: How Inequity Rigged the Economy and How to Change the Rules."
[83] "Renters in Foreclosure: Defining the Problem, Identifying Solutions." National Low Income Housing Coalition. 2008.

A study released this past July by the Pew Charitable Trusts, on the subject of downward economic mobility, finds that children of middle income families that live in high-poverty neighborhoods (defined as having a poverty level that exceeds 20 percent), compared with middle-income children living in low-poverty neighborhoods (poverty of less than 10 percent), have a greater than 50percent chance of downward mobility.[84]

According to the study, more than half of black children born between 1985 and 2000 whose families were at least middle-income were raised in high-poverty neighborhoods. On the other hand, only one percent of middle-income white children were raised in high-poverty neighborhoods. The study concludes that neighborhood poverty levels explain at least one-quarter to one-third of the black-white gap in downward mobility, more than the *combined* effects of parental education, family structure, occupation and labor force participation. These powerful and important findings drive home the significance of removing artificial barriers to housing choice that will only be achieved by purging discrimination from the housing markets.

There are three key implications for the future of fair housing that result from the current situation:

1. The wealth of millions of families of color is being destroyed, which will limit their ability to seek housing in non-segregated communities.

2. The credit scores of people of color are being undermined disproportionately, which will intensify the lack of access to a range of opportunities not limited to housing.

3. The damage to communities of color will further fuel segregation and unjust assumptions and myths about the livability of communities of color.

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[84] Sharkey, Patrick. "Neighborhoods and the Black-White Mobility Gap." Economic Mobility Project, Pew Charitable Trusts. July, 2009. Accessed online at http://www.pewtrusts.org/uploadedFiles/wwwpewtrustsorg/Reports/Economic_Mobility/PEW_SHARKEY_v12.pdf?n=1399.

Better FHA enforcement is necessary. The Federal Reserve has had regulatory jurisdiction over fair housing as it relates to financial institution lending activities, but its record on investigating and prosecuting potential fair housing violations is dismal. In fact, between 2004 and 2006, the Federal Reserve identified approximately 470 lenders whose practices were possibly in violation of civil rights and fair lending laws. Instead of investigating the lenders to determine the presence and extent of actual violations, the Federal Reserve referred all 470 cases to other regulatory agencies, and did not follow up when the other agencies similarly declined to investigate.[85] This is a dereliction of duty, particularly considering that the National Fair Housing Alliance estimates that more than four million acts of housing discrimination occur each year.

Lack of funding is a major contributor to poor oversight of fair-housing practices, but money is not the only cause. A lack of appropriate coordination among various agencies responsible for enforcing civil rights and equal opportunity, along with an inconsistent commitment to robust civil rights enforcement, has undermined progress on this essential national mandate. In fact, the Government Accountability Office reported in August that "[f]ederal enforcement agencies and depository institution regulators face challenges in consistently, efficiently, and effectively overseeing and enforcing fair lending laws due in part to data limitations and the fragmented U.S. financial regulatory structure."[86]

For these reasons, NCRC recommends the establishment of a cabinet-level agency focused on civil-rights enforcement. Empowering one agency to supervise the enforcement of all civil rights laws could greatly improve access to opportunities for millions of Americans whose only impediments are artificial walls and unfair and illegal impediments.

The secretary or chairperson of such an agency should report directly to the President of the United States and be responsible for measuring, monitoring, and eliminating discrimination from the public and private sectors. The agency would promote financial inclusion and racial equality

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[85] Inside Regulatory Strategies. November 14, 2005, Page 2. See also: Adler, Joe. "Big Increase in Lenders with Suspect HMDA Data." *American Banker*. September 11, 2006.
[86] "Fair Lending: Data Limitations and the Fragmented U.S. Financial Regulatory Structure Challenge Federal Oversight and Enforcement Efforts." U.S. Government Accountability Office. August 2009. Accessed online at: http://www.house.gov/list/press/financialsvcs_dem/gao.pdf.

by coordinating the civil rights offices that currently act without cohesion or unity across the different Cabinet departments. This would not usurp the role of agency-specific civil rights offices, but enable them to better achieve their missions by providing the tools, resources, and leveraging collective responsibility. Neither would this new agency supplant state-level civil rights agencies, with which it would work as a strategic partner.

The major advantage of a Cabinet-level civil rights agency would be to create cross-departmental exchanges of ideas, expertise, information, and goals. When a department fails to carry out civil rights enforcement mandates or does so haphazardly, the new agency would be able to compel improved enforcement. Finally, the symbolic value and ability of a civil rights agency to influence national attitudes about and behaviors regarding fair lending, fair housing, and civil rights in general should not be underestimated.

HUD, the Department of Justice, and all other federal agencies with fair housing responsibilities would be required to report to the new agency annually the number of fair housing and fair lending investigations, types of investigations, and outcomes. Annual reporting should include information on fair lending compliance exams conducted in conjunction with CRA exams.

The proposed Consumer Financial Protection Agency to consolidate the regulation of consumer financial products models many of the principles of NCRC's recommendation for a Cabinet-level civil rights agency to enforce the nation's civil rights laws. We continue to feel, however, that a dedicated civil rights enforcement coordinator is necessary in addition to a consumer rights coordinator.

Equality is Not Only about Justice

The issue of discrimination has been traditionally argued solely on the basis of fairness, equality, and justice. While those are important grounds, there is increasingly another critical reason to level the playing field by race and ethnicity. Within the next 35 years, half of the U.S. population will consist of people of color. This has particular implications for the American economy

overall since people of color, the fastest-growing share of the nation's population, are the least well-housed, have the most limited access to the labor and financial markets, and are disproportionately isolated from quality education and health care, and accumulate relatively low levels of wealth.

Globalization represents competitive challenges that America has never previously experienced. Growing concern over the considerable domestic job losses and the tenuous nature of the economic recovery in the U.S. are raising critical discussions on where job growth will occur in the U.S. in coming years.

Increased investments in training and higher education are the keys to the emerging knowledge economy. But as President Obama stated in a speech delivered March 10, 2009 before the National Hispanic Chamber of Commerce, "despite resources that are unmatched anywhere in the world, we've let our grades slip, our schools crumble, our teacher quality fall short, and other nations outpace us…and year after year, a stubborn gap persists between how well white students are doing compared to their African American and Latino classmates."[87]

If America is to continue to be an economic, political, and intellectual superpower as it moves forward into the twenty-first century, the old paradigm of discrimination and inequality must fall. All Americans must be prepared and allowed to compete. Americans must continue the open dialogue on race that began last year and fully understand the historical implications for our nation's future. Succeeding in a new, globalized, highly competitive world is not an option; it is an imperative.

Laying the Foundations for the Next Crisis

Rather than honestly identifying and directly addressing the causes of the financial system meltdown, there are signs that current interventions are simply laying the foundations for the

[87] Transcript available online at: http://www.nytimes.com/2009/03/10/us/politics/10text-obama.html.

next crisis before we emerge from the crisis in progress. Although Federal Reserve interventions have been successful in avoiding a more damaging financial system meltdown, the extraordinary financial support for the banking system, with so few restrictions on financial firms' activities, may create an even larger crisis down the road.

On the first anniversary of the fall of Lehman Brothers, rather than actively examining how best to address the challenges of "too big to fail" the financial system rescue has made too big – bigger. Four of the largest banks today, for example, issue half of all home loans and issue two of every three credit cards according to an analysis of federal data by the *Washington Post*.[88] Similarly, the government is financing ninety percent of all new mortgages.[89]

Even financial analysts and bankers themselves recognize the dangers of our current path. In a recent *Bloomberg News* interview, Richard Bernstein, CEO of Bernstein Capital Management LL, said "one year later, policymakers haven't learned the lesson of the [Lehman Brothers] bankruptcy." He went on to critique the government's response of allowing large firms to continue operating at their current size without implementing new regulatory processes to manage systemic risk. It "practically invites another catastrophe," he said.[90]

Jeff Rosenberg, the chief credit specialist at Bank of America Securities, said in an interview with Bloomberg Television that "there are parts of the credit markets that are back to the peak of credit bubble pricing." He went on to say that, "an unintended consequence of the Federal Reserve's actions to stabilize markets [is that] you end up just simply reflating the bubble for the next term."[91]

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[88] Cho, David. "Banks too Big to Fail Have Grown Even Bigger." *Washington Post.* August 28, 2009.
[89] Andrews, Edmund L. and David Sanger. "U.S. is Finding Its Role in Business Hard to Unwind." *New York Times*. September 13, 2009.
[90] Ivry, Bob, Christine Harper, and Mark Pittman. "Missing Lehman Lesson of Shakeout Means Too Big Banks May Fail." *Bloomberg News*. September 8, 2009. Accessed online at http://www.bloomberg.com/apps/news?pid=20601170&sid=aX8D5utKFuGA.
[91] "Bank of America's Rosenberg Interview on Credit Markets." *Bloomberg Television.* Aired August 10, 2009. Accessed August 14, 2009 at www.bloomberg.com/tvradio/tv.

Joseph Stiglitz voiced a similar view last week, saying, "The problems [in the banking system] are worse than they were in 2007 before the crisis."[92]

Conclusion

In conclusion, this is a distinct moment in history. The question is: Will we use it productively or will we squander it?

The answer to this question is not inconsequential. Much is at stake with respect to how honest we are in (1) analyzing what happened, (2) adopting immediate remedies to mitigate the damage, and (3) instituting long-range measures to ensure this type of crisis does not again occur.

Unfortunately, in all three areas, the early results are not promising. Despite a massive bailout of the financial institutions, the system remains precariously balanced on the edge of failure. Consumers continue to struggle through a virtual sea of deceptive debt and financial firms remain unaccountable to the American public.

Now is the time to enact strong legislation that will more directly and substantially help families avoid foreclosure on their homes.

Now is the time to enact meaningful legislation to ensure that financial firms work to promote the economic well being of the American public.

Now is the time to rebuild communities harmed by excessive foreclosures and severe levels of unemployment.

Now is the time to enforce the nation's civil rights laws.

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[92] Deen, Mark and David Tweed. "Stiglitz Says Banks Face Problems Bigger Than Pre-Lehman." *Bloomberg News*. September 13, 2009.

Now is the time for the American people to demand that this moment in history not be squandered.

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